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REPORT TO THE CONGRESS

Savings Available To
The Government By Timing
Advances' Of Loan And
Grant Funds With Actual
Cash Requirements'

B-114873

Farmers Home Administration
Department of Agriculture

BY THE COMPTROLLER GENERAL
OF THE UNITED STATES

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JULY 6, 1970



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D C 20548

B-114873

To the President of the Senate and the
Speaker of the House of Representatives

This is our report on savings available to the Government by timing advances of loan and grant funds with actual cash requirements, Farmers Home Administration, Department of Agriculture

Our review was made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67)

Copies of this report are being sent to the Director, Bureau of the Budget, and to the Secretary of Agriculture

A handwritten signature in dark ink, reading "James B. Stewart". The signature is written in a cursive style with a large initial "J".

Comptroller General
of the United States

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D I G E S T

WHY THE REVIEW WAS MADE

The Farmers Home Administration (FHA), under the Consolidated Farmers Home Administration Act of 1961, as amended, makes grants and direct and insured loans to public and nonpublic associations to finance the improvement and/or construction of rural water and sewer facilities. From 1961 through June 30, 1969, FHA advanced loan and grant funds of about \$809 million to about 3,850 associations. (See p. 6.)

The Government's general policy is to limit advances of loan and grant funds to recipients to amounts needed to meet their current requirements so as to preclude unnecessary borrowings by the U.S. Treasury and the related interest costs. The General Accounting Office (GAO) made a review to see if loan and grant funds under FHA's water and sewer program were being advanced to associations in accordance with this policy.

FINDINGS AND CONCLUSIONS

Contrary to Government policy, FHA's practice has been to advance loan and grant funds to associations under the water and sewer program without consideration of the associations' cash requirements.

In the case of loan funds, FHA instructions are directly contrary to Government policy. In the case of grant funds, FHA instructions are in accord with Government policy but were not followed by the FHA staff. (See p. 8.)

GAO analyzed the monthly cash balances of 92 associations. They had been advanced loan and grant funds of about \$43 million during August 1964 to October 1969 to finance the improvement and/or construction of water and sewer facilities in nine States. GAO found that generally FHA:

- had advanced the full amount of loans to associations even though substantial portions of such advances were not expended by the associations for periods up to 20 months or longer and
- had made one or more advances of grant funds to associations at times when the associations had substantial amounts of unexpended

loan and/or grant funds on hand. In some instances, the associations did not use substantial portions of the grant funds advanced for periods up to 15 months or longer.

The 92 associations maintained a combined average monthly cash balance of about \$11 million in excess of their cash requirements for an average period of 17 months--an average of about \$120,000 a month for each of the associations. GAO estimated that interest savings of about \$200,000 could have been realized by the Government if FHA had advanced the funds to the 92 associations only as needed. (See pp. 9 and 10.)

For fiscal year 1971, FHA expects to make loans and grants under the water and sewer program totaling about \$146 million to about 900 associations. If these funds are advanced on the basis of cash requirements, substantial savings in interest should be realized. (See p. 10.)

FHA instructions for making cash advances to association-type borrowers obtaining recreational loans, grazing loans, and irrigation loans are similar to the instructions for the water and sewer program. GAO did not make a review to determine the extent to which loan funds under these programs were being advanced ahead of the associations' actual needs; however, the Government policy of timing cash advances with actual cash requirements is also applicable to these loan programs.

For fiscal years 1968 and 1969, FHA made loans totaling about \$71 million to 663 associations under these programs. For fiscal year 1970, FHA expects to make loans totaling about \$14.6 million to 173 associations. (See p. 15.)

RECOMMENDATIONS OR SUGGESTIONS

FHA should revise its instructions to require that:

- cash advances under all association loan programs be made on the basis of the associations' anticipated cash requirements and
- associations furnish periodic estimates of project expenditures and such estimates be reviewed and analyzed by the FHA county supervisors for determining the amount of cash to be advanced.

FHA should also establish a program for systematically monitoring the advancing of loan and grant funds to associations to provide assurance that advances are made in accord with the associations' actual needs. (See pp. 15 and 16.)

AGENCY ACTIONS AND UNRESOLVED ISSUES

The Acting Administrator, FHA, stated that FHA was in general agreement with GAO's finding and recommendations. He stated also that:

--FHA has drafted procedural revisions relating to cash advances to all association-type borrowers which it believes will meet the objectives of GAO's recommendations and

--The revised procedures are being reviewed by the Department of Agriculture's Office of the General Counsel and will be put into effect as soon as practicable.

The Acting Administrator subsequently advised us that the advancing of loan and grant funds will be monitored after implementation of the revised procedures to ensure that the advances are properly made.

GAO plans to review FHA's revised procedures after they are issued to ascertain whether the procedures, if properly implemented, will provide adequate assurance that Government funds are advanced only as needed.

MATTERS FOR CONSIDERATION BY THE CONGRESS

GAO is bringing this matter to the attention of the Congress because of (1) the potential savings available to the Government by timing advances of loan and grant funds with actual cash requirements and (2) the continuing need for agencies to review their practices regarding advancing of funds to ensure that they are in accord with the general policy of the Government.

CHAPTER 1

INTRODUCTION

The General Accounting Office has examined into the procedures and practices followed by the Farmers Home Administration, Department of Agriculture, in advancing Government loan and grant funds to public and nonpublic associations to finance the improvement and/or construction of rural water and sewer facilities. We did not review the propriety of the loans and grants made by FHA or of the expenditures made by the associations from cash advanced to them. The scope of our review is described on page 17.

ORGANIZATION OF FHA

FHA was established on November 1, 1946, pursuant to the Farmers Home Administration Act of 1946 (60 Stat. 1062), to simplify and improve credit services available to farmers and to promote farm ownership. Pursuant to this act, the responsibility for administering various loan programs of predecessor agencies was delegated to the Administrator of the Farmers Home Administration by the Secretary of Agriculture.

FHA maintains 41 State offices--which serve the 50 States, the District of Columbia, Puerto Rico, and the Virgin Islands--and about 1,700 county offices. Each FHA State office is headed by an FHA State director who is responsible for all program operations within his territorial jurisdiction. The FHA county offices, each under the supervision of a FHA county supervisor, are located throughout the country ~~to serve~~ all agricultural ^{can be served} counties. Applications for all loans and grants are initially made to the county or State offices. County office operations are subject to review by the district supervisors or other State office officials.

Principal officials of the Department of Agriculture responsible for the administration of the matters discussed in this report are listed in appendix II.

STATUTORY AUTHORITY AND ADMINISTRATIVE REQUIREMENTS
FOR WATER AND SEWER LOANS AND GRANTS

FHA is authorized by section 306 of the Consolidated Farmers Home Administration Act of 1961, as amended (7 U.S.C. 1926), to make grants and direct and insured loans to public and nonpublic associations to finance the improvement and/or construction of water and sewer facilities which primarily serve farmers, ranchers, farm tenants and laborers, and other rural residents. With respect to grants, FHA instructions provide that grant assistance may be provided to an association when it is determined that the development cost of a project would result in excessive charges to users. Grant assistance is provided to reduce the associations' project costs to a level which will permit a reasonable user charge.

The 1961 act also provides that:

- water and sewer loans to associations be made at an interest rate not to exceed 5 percent per annum.
- loans be made only when FHA determines that associations are unable to obtain sufficient credit elsewhere to finance their actual needs at reasonable rates and terms.
- loans be repaid over a period not to exceed 40 years.
- the maximum principal loan indebtedness together with grant assistance not exceed \$4 million for any association at any one time, and
- the amount of grant assistance not exceed 50 percent of development costs of the water and/or sewer project.

FHA instructions provide, with certain exceptions, that water and sewer loans up to \$250,000 be approved by the FHA State director and loans of \$250,000 or more be approved by the FHA Administrator. FHA instructions provide also that development grants in excess of \$35,000 be approved by the FHA Administrator.

FHA instructions provide further that loan or grant funds advanced to associations be deposited in FHA-supervised bank accounts. These accounts are required to be established by the associations in banks of their choice under deposit agreements entered into by the associations, the banks, and FHA. Under such agreements, the deposits are assigned to FHA as security for payment of the indebtedness of the associations and withdrawals are permitted only by order of the associations and the counter signature of a representative of FHA on the basis of invoices or other evidence showing that costs associated with the purpose of the loan or grant have been incurred.

FHA records show that, from the inception of the water and sewer program in 1961 through June 30, 1969, FHA has advanced ~~loans and grants~~ ^{loans} funds totaling about \$719 million and \$90 million, respectively, to about 3,850 associations. For fiscal year 1971, FHA expects to make loans of about \$126 million and grants of about \$20 million to about 900 associations. To finance the improvement and/or construction of water and sewer facilities.

FINANCING OF FHA'S WATER AND SEWER PROGRAM

Direct loans are financed with Treasury borrowings and are made from FHA's Direct Loan Account up to a maximum amount established by the Congress in annual appropriation acts. Grant funds are appropriated annually by the Congress.

Insured loans to associations are made from FHA's Agricultural Credit Insurance Fund. After making these loans at an interest rate not to exceed 5 percent, FHA sells the association notes to private investors for periods ranging from 1 to 25 years and guarantees repayment of the loans. In order to make the notes attractive to private investors, FHA pays interest on the notes at rates that are competitive with interest rates being paid for private capital. At December 31, 1969, FHA was paying private investors interest on insured notes at rates ranging from 8.50 to 8.75 percent.

INTERNAL AUDITS OF FHA'S
WATER AND SEWER PROGRAM

The Office of the Inspector General, Department of Agriculture, has not made a detailed audit of FHA's water and sewer program. In fiscal year 1969 the Office made a survey of all FHA's association loan programs and identified weaknesses in FHA's management of these programs including the water and sewer program. Due in large measure to our audit of FHA's water and sewer program which was in progress in fiscal year 1969 and to our audit of other association loan programs, the Office decided to concentrate its audit effort on FHA's recreation loan program.

CHAPTER 2

SAVINGS AVAILABLE BY TIMING

ADVANCES OF LOAN

AND GRANT FUNDS WITH ACTUAL CASH REQUIREMENTS

Contrary to Government policy, FHA's practice has been to advance loan and grant funds to associations under the water and sewer program without consideration of the associations' cash requirements. In the case of loan funds, FHA instructions were directly contrary to Government policy. In the case of grant funds, FHA instructions were in accord with Government policy but were not followed by the FHA staff.

As a result of these practices, Government funds have been disbursed in advance of the time the funds were actually needed by the associations and thus accelerated Government borrowings and increased related interest costs.

GOVERNMENT POLICY OF TIMING CASH ADVANCES

Treasury Department Circular No. 1075 (revised), dated April 10, 1969, states that cash advances to recipient organizations (including State and local governments, educational institutions, international organizations, and any other public and private organizations) be limited to the minimum amounts needed and be timed to be in accord with the actual cash requirements of the organizations. The circular states also that, for relatively small operations where the aggregate annual advances are under \$250,000, cash advances to recipient organizations be made monthly or more frequently to meet current disbursement needs and that, for larger operations, the timing and amount of cash advances to recipient organizations be as close to actual daily disbursements as is administratively feasible.

ADVANCEMENT OF FUNDS PRIOR
TO ASSOCIATIONS' NEEDS

FHA's instructions concerning the advancement of funds to associations receiving water and sewer loans and grants provide that:

--the full amount of direct and insured loans be disbursed to the associations at the time of loan closing. Multiple advances must be justified and in no case will more than four advances be made.

--grant funds over \$20,000 be disbursed periodically in amounts the associations will expend within a 30-day period.

We selected 92 associations which had been advanced loan and grant funds of about \$43 million during the period August 1964 to October 1969 to finance the improvement and/or construction of rural water and sewer facilities in nine States and analyzed their monthly cash balances. In our selection of these associations, major considerations were (1) that an association received significant advances of loan and grant funds and (2) that a sufficient period of time elapsed since the association had received the advances to enable a determination of when the funds actually were needed. Our analysis showed that generally FHA:

--had advanced the full amount of loans to associations even though substantial portions of such advances were not expended by the associations for periods up to 20 months or longer and

--had made one or more advances of grant funds to associations even though the associations had substantial amounts of unexpended loan and/or grant funds on hand. In some instances, the associations did not use substantial portions of grant advances for periods up to 15 months or longer.

Our analysis showed also that the 92 associations had maintained a combined average monthly cash balance of about \$11 million in excess of their cash requirements for an average period of 17 months--an average of about \$120,000 a

month for each of the associations. We estimated that interest savings of about \$200,000 could have been realized by the Government if FHA had advanced the funds to the 92 associations only as needed.

The estimated interest savings of \$200,000 was computed

- for direct loan fund advances by applying the difference between the 5-percent rate the associations were paying on their loans and the average interest rate paid by the Treasury on all marketable securities to the amount of the advances in excess of the associations' requirements during each month,
- for grant fund advances by applying the average interest rate paid by the Treasury on all marketable securities to the amount of the advances in excess of the associations' requirements during each month, and
- for insured loan fund advances by applying the difference between the 5-percent rate the associations were paying on their loans and the rate of interest FHA paid private investors who bought the associations' notes to the amount of the advances in excess of the associations' requirements during each month.

At December 31, 1969, the average interest rate paid by the Treasury on all marketable securities was 5.849 percent. Also, at December 31, 1969, FHA was paying private investors annual interest on insured notes at rates ranging from 8.50 to 8.75 percent.

For fiscal year 1971, FHA expects to make loans and grants under the water and sewer program totaling about \$146 million to about 900 associations. If these funds are advanced on the basis of cash requirements, substantial savings in interest should be realized.

We believe that the following three examples illustrate FHA's practice of advancing funds to associations in excess of their cash requirements.

Association A

Association A in the State of North Carolina received a total of \$2,150,000 in FHA loan and grant funds for the construction of a water system. The following table shows the receipts and disbursements of these funds over a 23-month period and the unexpended balance of funds at the end of each month.

Year and month	<u>Funds received</u>		<u>Disburse-</u> <u>ments</u>	Balance of funds at end of month
	<u>Loan</u>	<u>Grant</u>		
1968:				
Jan.	\$631,250		\$ 81,356.27	\$ 549,893.73
Feb.			-	549,893.73
Mar.			75,387.44	474,506.29
Apr.			150,045.29	324,461.00
May			116,737.73	207,723.27
June			130,223.12	77,500.15
July		\$200,000	68,241.90	209,258.25
Aug.			34,582.83	174,675.42
Sept.			59,998.04	114,677.38
Oct.			41,775.80	72,901.58
Nov.			48,742.40	24,159.18
Dec.	950,000	200,000	82,988.14	1,091,171.04
1969:				
Jan.		168,750	94,772.50	1,165,148.54
Feb.			69,694.27	1,095,454.27
Mar.			60,018.81	1,035,435.46
Apr.			54,244.28	981,191.18
May			186,287.50	794,903.68
June			103,147.98	691,755.70
July			66,289.37	625,466.33
Aug.			109,220.41	516,245.92
Sept.			46,789.18	469,456.74
Oct.			72,088.26	397,368.48
Nov.			103,678.36	293,690.12 ^a

^aUnexpended funds at the time we completed our fieldwork.

For the 23-month period, the average monthly balance of FHA funds in excess of the association's cash needs was about \$500,000. We estimated that interest savings of about

\$28,000 could have been realized by the Government if FHA had advanced these funds only as needed by the association.

Association B

Association B in the State of Washington received a total of \$244,000 in FHA loan and grant funds for the construction of a sewer system. The following table shows the receipts and disbursements of these funds over a 22-month period and the unexpended balance of funds at the end of each month.

Year and month	<u>Funds received</u>		<u>Disburse- ments</u>	<u>Balance of funds at end of month</u>
	<u>Loan</u>	<u>Grant</u>		
1968:				
Jan.	\$150,000		\$ -	\$150,000.00
Feb.			19,061.77	130,938.23
Mar.			7,691.98	123,246.25
Apr.			-	123,246.25
May			65,422.63	57,823.62
June			-	57,823.62
July		\$94,000	57,866.94	93,956.68
Aug.			-	93,956.68
Sept.			40,380.46	53,576.22
Oct.			19,396.26	34,179.96
Nov.			-	34,179.96
Dec.			-	34,179.96
1969:				
Jan.			7,539.65	26,640.31
Feb.			-	26,640.31
Mar.			-	26,640.31
Apr.			-	26,640.31
May			-	26,640.31
June			-	26,640.31
July			4,042.04	22,598.27
Aug.			-	22,598.27
Sept.			-	22,598.27
Oct.			-	22,598.27 ^a

^aUnexpended funds at the time we completed our fieldwork.

For the 22-month period, the average monthly balance of FHA funds in excess of the association's cash needs was about \$50,000. We estimated that interest savings of about \$2,000 could have been realized by the Government if FHA had advanced these funds only as needed by the association.

Association C

Association C in the State of Mississippi received a total of \$1,294,000 in FHA loan funds for the construction of a water system. The following table shows the receipt and disbursements of these funds over a 21-month period and the unexpended balance of funds at the end of each month.

<u>Year and month</u>	<u>Loan funds received</u>	<u>Disbursements</u>	<u>Balance of funds at end of month</u>
1968:			
Feb.	\$1,294,000.00	\$ 35,426.75	\$1,258,573.25
Mar.		-	1,258,573.25
Apr.		58,941.79	1,199,631.46
May		44,556.79	1,155,074.67
June		73,808.32	1,081,266.35
July		69,048.40	1,012,217.95
Aug.		117,362.96	894,854.99
Sept.		152,366.42	742,488.57
Oct.		62,246.98	680,241.59
Nov.		91,309.99	588,931.60
Dec.		61,154.00	527,777.60
1969:			
Jan.		30,000.00	497,777.60
Feb.		95,991.13	401,786.47
Mar.		6,476.10	395,310.37
Apr.		92,693.69	302,616.68
May		133,892.03	168,724.65
June		42,866.26	125,858.39
July		28,295.58	97,562.81
Aug.		12,676.38	84,886.43
Sept.		-	84,886.43
Oct.		51,154.19	33,732.24 ^a

^aUnexpended funds at the time we completed our fieldwork.

For the 21-month period, the average monthly balance of FHA funds in excess of the association's cash needs was about \$575,000. We estimated that interest savings of about \$14,000 could have been realized by the Government if FHA had advanced these funds only as needed by the association.

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Our review was directed primarily toward examining into the practices followed by FHA in approving cash advances to associations under the water and sewer program. We noted, however, that FHA instructions require that similar procedures be followed in making cash advances to association-borrowers obtaining recreational loans, grazing loans, and irrigation loans. We did not make a review of these loan programs to determine the extent to which loan funds were being advanced ahead of the associations' actual needs; however, the Government's policy of timing cash advances with actual cash requirements is also applicable to these programs. For fiscal years 1968 and 1969, FHA made loans to 663 associations under these programs totaling about \$71 million, and, for fiscal year 1970, FHA expects to make loans to 173 associations totaling about \$14.6 million.

CONCLUSIONS

On the basis of our review, we concluded that FHA should revise its practices and instructions for advancing loan and grant funds to recipients to achieve the objective of the Government's policy of timing cash advances with the recipients' actual needs. We believe that, in accomplishing this objective, FHA should require the associations to submit periodic estimates of their cash needs and that FHA should review and analyze such estimates for determining the amount of cash to be advanced.

We believe also that, by more accurately timing advances of loan and grant funds with the recipients' actual needs, particularly since rates on Government borrowings have increased significantly in recent years, FHA can improve its management of funds and make a contribution toward reducing Government interest costs.

RECOMMENDATIONS

We recommend that the Administrator, FHA, have the agency's instructions revised to require that:

- cash advances under all association loan programs be made on the basis of the associations' anticipated cash requirements and
- the associations furnish periodic estimates of project expenditures and such estimates be reviewed and analyzed by the FHA county supervisors for determining the amount of cash to be advanced.

We recommend also that the Administrator require that a program be established for systematically monitoring the advancing of loan and grant funds to associations to provide assurance that advances are made in accord with the associations' actual needs.

AGENCY COMMENTS

The Acting Administrator, FHA, advised us by letter dated March 5, 1970 (see app. I), that FHA was in general agreement with our finding and recommendations. He stated that:

- FHA has drafted procedural revisions relating to cash advances to all association-type borrowers which it believes will meet the objectives of GAO's recommendations and
- the revised procedures are being reviewed by the Department of Agriculture's Office of the General Counsel and will be put into effect as soon as practicable.

The Acting Administrator subsequently advised us that the advancing of loan and grant funds will be monitored after implementation of the revised procedures to ensure that the advances are properly made.

We plan to review FHA's revised procedures after they are issued to ascertain whether the procedures, if properly implemented, will provide adequate assurance that Government funds are advanced only as needed. We believe that audits by the Office of the Inspector General, Department of Agriculture, could provide assurance to FHA that funds are advanced to associations only as needed.

CHAPTER 3

SCOPE OF REVIEW

Our review was made at the FHA headquarters office in Washington D.C.; and at the FHA State offices at Little Rock, Arkansas; Gainesville, Florida; Atlanta, Georgia; Orono, Maine; Jackson, Mississippi; Raleigh, North Carolina; Portland, Oregon; and Wenatchee, Washington. Each State office is responsible for FHA activities in one or more States.

We reviewed the pertinent policies and procedures under which FHA advances Government loan and grant funds to public and nonpublic associations to finance the improvement and/or construction of rural water and sewer facilities. Also, we reviewed the policies followed by FHA under its other association loan programs for advancing funds to associations obtaining grazing loans, recreational loans, and irrigation loans.

We examined records pertaining to the supervised bank accounts of 92 associations in 9 States--10 in Arkansas; 13 in Florida; 8 in Georgia; 10 in Maine, 10 in Mississippi; 13 in North Carolina; 11 in Oregon; 7 in Vermont; and 10 in Washington.

APPENDIXES

UNITED STATES DEPARTMENT OF AGRICULTURE
FARMERS HOME ADMINISTRATION
WASHINGTON D C 20250

OFFICE OF THE ADMINISTRATOR

MAR 5 1970

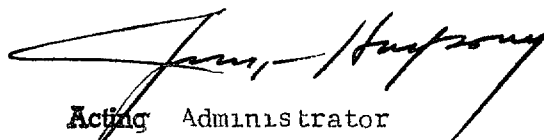
Mr. Victor L. Lowe
Associate Director
General Accounting Office
Washington, D. C.

Dear Mr. Lowe:

We have reviewed your draft report on savings available to the Government by timing cash advances with actual cash requirements, and we have discussed certain aspects of it with members of your staff.

We are in general agreement with the finding and recommendations in the draft report and we have drafted procedural revisions relating to cash advances to all association-type borrowers. We believe that our revised procedures will meet the objectives of your recommendations. The proposed procedures, which are now being reviewed by the Department's Office of the General Counsel, will be put into effect as soon as practical.

Sincerely,


Acting Administrator

BEST DOCUMENT AVAILABLE

PRINCIPAL OFFICIALS OF THE DEPARTMENT OF AGRICULTURE
RESPONSIBLE FOR THE ADMINISTRATION OF THE MATTERS
DISCUSSED IN THIS REPORT

	<u>Tenure of office</u>	
	<u>From</u>	<u>To</u>
SECRETARY OF AGRICULTURE:		
Clifford M. Hardin	Jan. 1969	Present
Orville L. Freeman	Jan. 1961	Jan. 1969
ASSISTANT SECRETARY OF AGRICULTURE FOR RURAL DEVELOPMENT AND CON- SERVATION:		
Thomas K. Cowden	Apr. 1969	Present
John A. Baker	Mar. 1961	Jan. 1969
ADMINISTRATOR, FARMERS HOME ADMIN- ISTRATION:		
James V. Smith	Jan. 1969	Present
Howard Bertsch	Apr. 1961	Jan. 1969